



Please contact any of the following attorneys if you have questions regarding this Independent School Law Alert.

**Caryn G. Pass**  
[cypass@venable.com](mailto:cypass@venable.com)  
202.344.8039

**Heather J. Broadwater**  
[hjbroadwater@venable.com](mailto:hjbroadwater@venable.com)  
202.344.8042

**Grace H. Lee**  
[ghlee@venable.com](mailto:ghlee@venable.com)  
202.344.8043

**Elizabeth S. Snodgrass**  
[essnodgrass@venable.com](mailto:essnodgrass@venable.com)  
202.344.4352

## The New Form 990: Is Your School Ready?

By Grace H. Lee

Recently, the IRS released the final draft of the new Form 990, to be effective for the 2008 filing. Particularly interesting to independent schools is the inclusion of Part VI: Governance, Management, and Disclosure. This new section, which seeks information regarding schools' governing bodies and policies, reflects the IRS' increased scrutiny of tax-exempt organizations and gives insight as to the IRS' perception of good governance in such organizations. Although schools are not required to maintain many of the policies and procedures addressed in Part VI, they promote good governance and help ensure compliance with tax laws.

### Board Minutes

Section A of Part VI asks whether the organization contemporaneously documented the meetings held or written actions undertaken during the year by the governing body and each committee with authority to act on behalf of the governing body. An independent school's bylaws should call for minutes to be taken of each meeting of the board of trustees and its committees. If the bylaws do not so provide, now may be the time for an amendment. At the very least, however, boards and committees should institute the practice of keeping minutes of their proceedings.

### Conflicts of Interest Policy

The new Form 990 asks whether the organization has a written conflict of interest policy. In order to answer "yes" to this question, a school should have a conflict of interest policy that defines what constitutes a conflict of interest, identifies the classes of individuals within the school that are covered by the policy, facilitates disclosure of information that may help identify conflicts of interest, and specifies procedures that the school follows in managing conflicts of interest. In addition to the conflict of interest policy, the new Form 990 asks whether officers, directors, trustees and key employees are required to disclose or update annually (or more frequently) the existence of interests that could give rise to conflicts of interest on their part. Schools must also disclose whether they regularly and consistently monitor and enforce compliance with the policy, and describe the process for enforcement. If your independent school does not currently operate under a conflict of interest policy, with an annual disclosure requirement, you are well-advised to enact and enforce one.

### Whistleblower Policy

The new Form 990 asks schools to disclose whether they have a whistleblower policy. In order for a school to be able to answer "yes" to this question, the school's whistleblower policy should encourage faculty, staff, and volunteers to come forward with credible information on illegal practices or violations of school policies. The Sarbanes-Oxley Act of 2002 ("SOX") imposes criminal penalties for taking action in retaliation against those who report a suspected federal offense to a law enforcement agency. The new Form 990's questions regarding the written whistleblower policy reach farther, however, than mere compliance with SOX; the IRS encourages each organization to have a policy for handling employee complaints and the confidential reporting of any suspected financial impropriety or misuse of assets. The existence of such a policy helps the governing board and senior management become aware of and address any issues before serious harm is done to the school.

### Document Retention and Destruction Policy

The new Form 990 asks whether the school maintains a written document retention and destruction policy. Such a policy should identify the responsibilities of staff, *volunteers*, board members, and outsiders for maintaining and documenting the storage and destruction of the organization's documents and records. SOX makes it a crime to destroy documents to prevent their use in an official proceeding. The type of policy contemplated by the new Form 990 goes beyond the requirements of SOX, and implies that every independent school should have a written document retention and destruction policy to be able to document its compliance with SOX.

### Compensation

New attention is focused on the process by which compensation arrangements for employees of tax-exempt organizations are determined, using the safe harbor provisions under intermediate sanctions rules as the standard for proper governance. In order to meet the standards of the new Form 990, schools must include the following elements for their compensation analysis: (1) Review and approval by a governing body or compensation committee, provided that persons with a conflict of interest with respect to the compensation arrangement at issue were not involved; (2) Reliance by the persons making the compensation decision upon comparability data as to compensation arrangements for similarly qualified persons in functionally comparable positions at similarly situated schools; and (3) Contemporaneous documentation and recordkeeping with respect to deliberations and decisions regarding the compensation arrangement.

Schedule J of the new Form 990 also expands the group of employees for whom compensation has to be reported and requires greater detail about their compensation packages. Reporting applies to officers, directors, trustees, key employees, and the five highest compensated employees (other than officers or key employees). In addition to currently taxable base compensation, schools must also report various nontaxable welfare and fringe benefits, bonus and incentive compensation, nonqualified deferred compensation, equity based compensation, compensation based on revenues or net earnings, severance arrangements, various other fringe benefits such as first-class travel, tax indemnifications and gross-ups, housing, and club dues, and compensation from both related and unrelated organizations.

#### **Joint Venture Policy**

If during the tax year, the school invested in, contributed assets to, or otherwise participated in a joint venture or similar arrangement with another entity, it must disclose this on the new Form 990. The Form 990 also asks whether the school has a written policy or procedure that helps determine that its participation is in accordance with federal tax law and that it has taken steps to safeguard its exempt status with respect to its participation in the joint venture.

Independent schools should identify which policies and procedures they currently have in place and analyze them in light of the reporting requirements imposed by the new Form 990. Policies and procedures must be in place by the end of the school's tax year in order for a school to be able to indicate on the new Form 990 that such policies and procedures exist. Accordingly, schools should take steps now to prepare for filing the new Form 990.

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